

Hall & Wilcox Webinar Property Funds Association

Fees and Costs Regulatory Update
2 July 2020

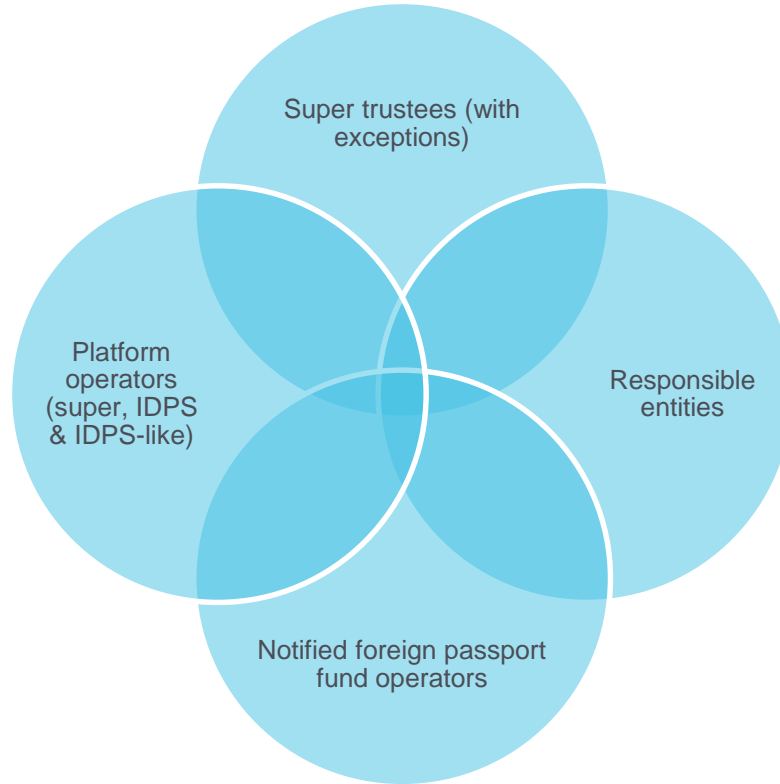
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What we will discuss

1. Background
2. Regulatory infrastructure
3. Key wins
4. Key new concepts
5. Transition period
6. Current issues

Focus is on managed investment schemes and not super funds or platforms

To whom does the RG 97 regime apply?



A short history

Date	Item
2002-2004	Financial Services Reform Act 2001 ('FSR') – 'PDS' and original fees and costs disclosure regime
2005	'Enhanced' fee disclosure regime in Schedule 10 to the Corporations Regulations
2010	Shorter PDS regime
2013	Legislative change to Schedule 10 for super products
July 2014	REP 398 – need to report indirect costs; need to capture some T&O costs as management costs; perf fees disclosure practices; identifies 'fee gaming' as an issue
December 2014	Class Order [CO 14/1252] & RG 97
2015 to 2017	Amendments to class order
2016+	Website 'Questions and Answers'
March 2017	Revised RG 97
November 2017	Announcement of review and appointment of independent expert (Darren McShane)
July 2018	Report 581 <i>Review of ASIC Regulatory Guide 97 Disclosing fees and costs in PDSs and periodic statements</i> (independent review report)
January 2019	Consultation Paper 308 <i>Review of RG 97 Disclosing fees and costs in PDSs and periodic statements</i>
November 2019	New regime - ASIC <i>Corporations (Disclosure of Fees and Costs) Instrument 2019/1070</i> and RG 97
May 2020	Announcement - Opt-in to new regime 30 September 2020 and must comply by 30 September 2022

Current infrastructure

Current	New
Schedule 10 as modified by ASIC Class Order [CO 14/1252]	ASIC Corporations (Disclosure of Fees and Costs) Instrument 2019/1070
RG 97	Revised RG 97
Q&A	

Does it matter?

'It's time to 'call time' on disclosure as the default consumer protection. It's not the 'silver bullet' once thought, nor should it be relied upon as one. **Disclosure can and has backfired** in unexpected and harmful ways....

Ideally this report will be a must read for corporate Australia, especially financial firms with near term **design and distribution obligations.**'

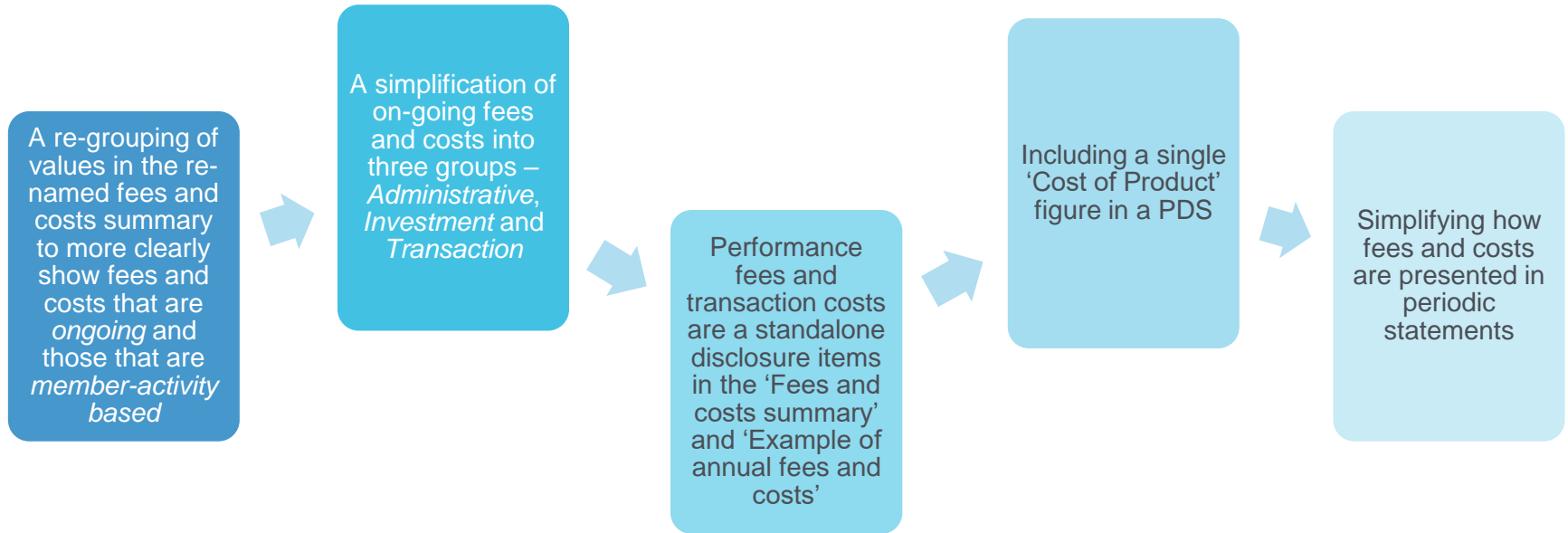
ASIC Deputy Chair, Karen Chester, in launching REP 632 *Disclosure: Why it shouldn't be the default*

RG 97 and DDO?

‘Disclosure **may also be useful** for some consumers in some contexts. For example, consumers can use disclosure of fees and costs post-purchase for reference in the event of a dispute. Disclosure alone is, however, not sufficient to drive good consumer outcomes. We encourage you to **consider the outcomes for consumers** who invest in the products you offer and **design** both the fees and costs themselves, and the information you provide about those fees and costs, to support good outcomes. For example, this could involve simplifying fees and costs to minimise consumer confusion.’

RG 97.6 (November 2019)

Key amendments



Other key features

Differences between MIS and Super remain

Removing the indirect cost ratio concept

Maintain the status quo for the treatment of derivative financial products but align with other amendments regarding transaction costs

Shorter PDS has long-form Fees and costs summary

Changing the structure and content of RG 97 (see revised RG 97)

Minor drafting amendments to Schedule 10 to improve clarity

Key wins

Removing any distinction between performance fees and performance-related fees

Performance fees to be calculated as the average of performance fees in the previous five financial years, and not just the previous financial year

Property operating costs, borrowing costs, implicit transaction costs or market impact costs do not need to be disclosed in PDSs or periodic statements

Disclosures in periodic statements are simplified

Disclosure of 'counterparty spreads' as a separate line item in the 'Fees and costs summary' (as newly re-named) and 'Example of annual fees and costs' are not required

Overall principle of not being misleading is evident in RG 97 guidance, which overrides legalism

Key changes to terminology

Current	New regime
'Management costs'	'Management fees and costs'
'Transactional and operational costs'	'Transaction costs', which exclude certain 'excluded transactional and operational costs'
'Fees and costs template'	'Fees and costs summary'
N/A	'Cost of product information'

Basic structure of fees and costs disclosure in long-form PDSs

Current	Proposed
Consumer advisory warning	Consumer advisory warning
Preamble to fees and costs template	Preamble to fees and costs summary
Fees and costs template	<u>Fees and costs summary</u>
Example of annual fees and costs	Example of annual fees and costs
N/A	<u>Cost of product information</u>
Additional explanation of fees and costs	Additional explanation of fees and costs

Consumer advisory warning

DID YOU KNOW?

Small differences in both investment performance and fees and costs can have a substantial impact on your long-term returns.

For example, total annual fees and costs of 2% of your account balance rather than 1% could reduce your final return by up to 20% over a 30-year period (for example reduce it from \$100,000 to \$80,000).

You should consider whether features such as superior investment performance or the provision of better member services justify higher fees and costs.

You may be able to negotiate to pay lower ~~contribution fees and management costs where applicable.~~ Ask the fund or your financial adviser.

TO FIND OUT MORE

If you would like to find out more, or see the impact of the fees based on your own circumstances, the **Australian Securities and Investments Commission (ASIC)** website (www.moneySMART.gov.au) has a managed funds fee calculator to help you check out different fee options.

MIS Fees and costs table – before and after

[Name of collective investment product]		
Type of fee or cost	Amount	How and when paid
Fees when your money moves in or out of the product		
<i>Establishment fee</i> The fee to open your investment		
<i>Contribution fee</i> ¹ The fee on each amount contributed to your investment		
<i>Withdrawal fee</i> ¹ The fee on each amount you take out of your investment		
<i>Exit fee</i> ¹ The fee to close your investment		
Management costs		
<i>The fees and costs for managing your investment</i> ¹ The amount you pay for specific investment options is shown at page [insert page number]		
Service fees ²		
<i>Switching fee</i> The fee for changing investment options		

- This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional Explanation of Fees and Costs”.)
- [If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]

Fees and costs summary[¶]

[Name of collective investment product] [□]		
Type of fee or cost [□]	Amount [□]	How and when paid [□]
Ongoing annual fees and costs[□]		
<i>Management fees and costs</i> [¶] The fees and costs for managing your investment ^{2□}	□	□
<i>Performance fees</i> [¶] Amounts deducted from your investment in relation to the performance of the product [□]	□	□
<i>Transaction costs</i> [¶] The costs incurred by the scheme when buying or selling assets [□]	□	□
Member activity related fees and costs (fees for services or when your money moves in or out of the scheme)^{1□}		
<i>Establishment fee</i> [¶] The fee to open your investment [□]	□	□
<i>Contribution fee</i> ^{2¶} The fee on each amount contributed to your investment [□]	□	□
<i>Buy-sell spread</i> [¶] An amount deducted from your investment representing costs incurred in transactions by the scheme [□]	□	□
<i>Withdrawal fee</i> ^{2¶} The fee on each amount you take out of your investment [□]	□	□
<i>Exit fee</i> ^{2¶} The fee to close your investment [□]	□	□
<i>Switching fee</i> [¶] The fee for changing investment options [□]	□	□

- [If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional explanation of fees and costs”.][¶]
- This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional explanation of fees and costs”.)[¶]

Fees and costs summary – additional features

Show negative performance fees by stating 'See Additional explanation of fees and costs' in the 'Amount' column of the Fees and costs summary

Abbreviated fees and costs template in a shorter PDS replaced with long-form PDS Fees and costs summary

ASIC appears not to allow management fees and costs to be broken down into different components – eg base management fee and indirect costs:
RG 97.357

Example of annual fees and costs

Example of annual fees and costs for a balanced investment option or other investment option

This table gives an example of how the ongoing annual fees and costs in the balanced investment option for this product can affect your investment over a 1- year period. You should use this table to compare this product with other products offered by managed investment schemes.

EXAMPLE—the Balanced Investment Option EXAMPLE— <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i>		BALANCE OF \$50,000 WITH A CONTRIBUTION OF \$5,000 DURING YEAR
Contribution Fees	0-4% <input type="checkbox"/>	For every additional \$5,000 you put in, you will be charged between \$0 and \$200. <input type="checkbox"/>
PLUS Management Costs fees and costs	1-3% <input type="checkbox"/>	And , for every \$50,000 you have in the <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i> you will be charged \$650. <input type="checkbox"/>
PLUS Performance fees	<input type="checkbox"/>	And , you will be charged \$ <input type="checkbox"/> in performance fees each year
PLUS Transaction costs	<input type="checkbox"/>	And , you will be charged \$ <input type="checkbox"/> in transaction costs
EQUALS Cost of <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i>		If you had an investment of \$50,000 at the beginning of the year and you put in an additional \$5,000 during that year, you would be charged fees of from: \$650<input type="checkbox"/> to \$850*<input type="checkbox"/> ¹ What it costs you will depend on the investment option you choose and the fees you negotiate.

* Additional fees may apply:

Establishment fee—\$50—\$

And, if you leave the managed investment scheme early, you may also be charged **exit fees** of between 0 and 5% % of your total account balance (between \$0 and \$2,500. for every \$50,000 you withdraw).

Cost of product

Cost of product for 1 year

The cost of product gives a summary calculation about how ongoing annual fees and costs can affect your investment over a 1-year period for all investment options. It is calculated in the manner shown in the Example of annual fees and costs.

The cost of product assumes a balance of \$50,000 at the beginning of the year with a contribution of \$5,000 during the year. (Additional fees such as an establishment fee or an exit fee may apply: refer to the Fees and costs summary for the relevant option.)

You should use this figure to help compare this product with other products offered by managed investment schemes.

<i>[insert name of investment option]</i>		Cost of product \$[]
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- Idea is to show abbreviated fees and costs of other investment options in the PDS
- Calculation methodology same as Example of annual fees and costs
- **Not required where PDS relates only to one investment option**

Transaction costs

Include:

- Brokerage
- Buy-sell spread
- Settlement (and custody) costs
- Clearing costs
- Stamp duty
- Costs of derivative financial products used for hedging
- Transaction costs of interposed vehicles

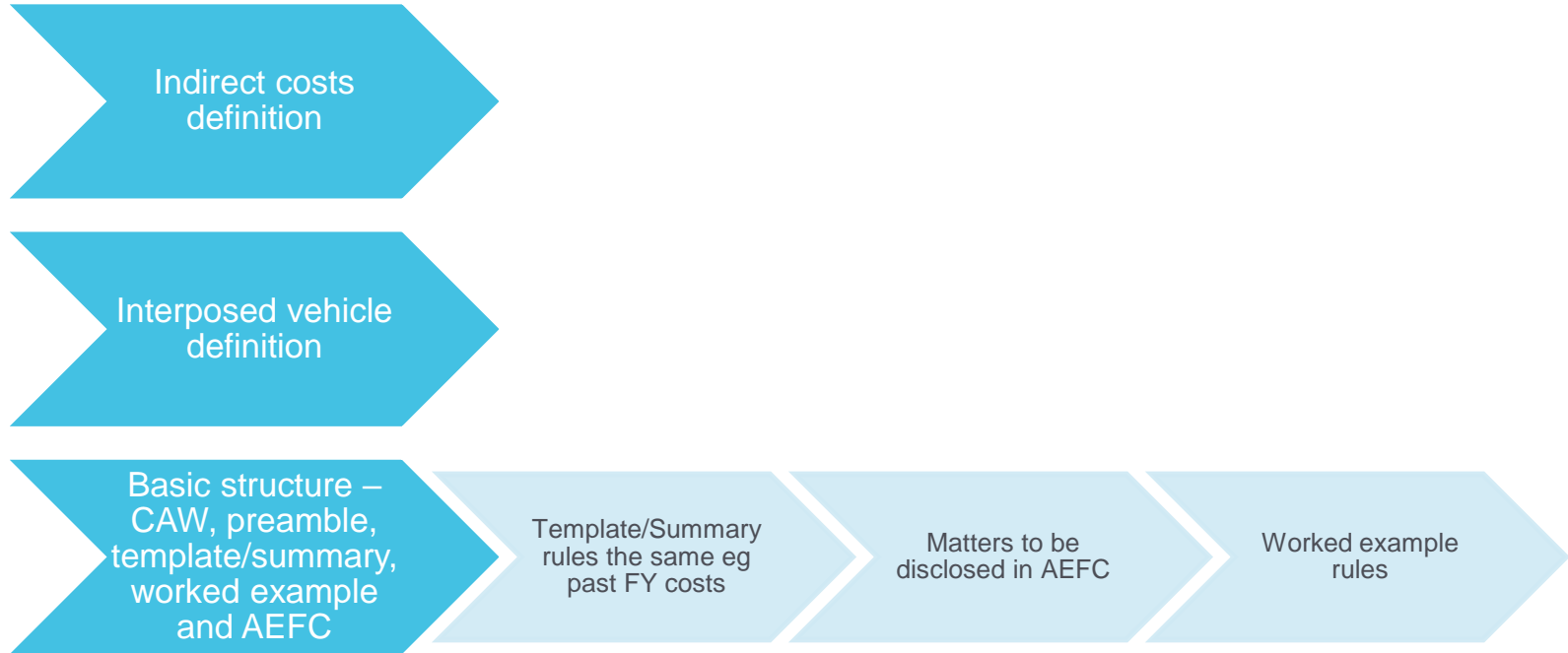
Exclude:

- 'Excluded transactional and operational costs'
- Costs otherwise charged as (relevantly) management fees and costs
 - borrowing costs
 - property operating costs
 - 'implicit transaction costs or market impact costs' – eg:
 - Unlisted assets: acquisition price less (spot) sale price ['bid-ask spreads'];
 - Listed assets: acquisition price less (spot) bid price ['difference in price between decision to trade and execution of trade']

} Implicit T&O costs excluded

In Fees and Costs Summary and Example of Annual Fees and Costs, transaction costs disclosed net of any buy-sell spread recovered

Things remaining substantially the same



Updated regulatory guide – some helpful points

- Clarity that fees for asset consultants and valuations are management fees and costs: RG 97.154(c)
- Expanded examples of where the Example of fees and costs can be adapted: RG 97.169-171
- For a shorter PDS, no need to include Example of annual fees and costs in full Sch 10 disclosure (in incorporated material) – but silent on the CAW: RG 97.207
- Table 5 shows clear rules for calculating management fees and costs
- Table 6 shows clear rules for calculating transaction costs
- Transaction costs examples: due diligence costs; sales commissions; legal, advisory and professional costs; failed deal costs: RG 97.333

Updated regulatory guide – some lost opportunities or ambiguities

- Not much useful guidance on exclusion for costs relating to a specific asset or activity that an investor would incur if they invested directly in the asset: cl 102(2)(h): RG 97.153
- Management fees and costs include RE overheads: RG 97.154(e)
- No specific guidance on mortgage funds – the example of costs paid by a super trustee's related party (RG 97.268) is not analogous costs paid by a borrower
- ASIC appears not to allow management fees and costs to be broken down into different components – eg base management fee and indirect costs: RG 97.357
- Some ambiguous drafting

Transition period

PDSs

Current transition period

- New regime applies to PDSs issued on or after 30 September 2020; and
- There is **no ability to 'opt-in' early**

Announced revised transition period

- **May 'opt-in'** to new regime on or after 30 September 2020
- **Must comply** by 30 September 2022 for PDSs given after that date

Periodic statements

- Periodic statements (ongoing or on exit) for a reporting period that commences on or after 1 July 2021
- Issuers **may 'opt-in'** to the updated periodic statement requirements if the periodic statement is for a reporting period that:
 - commences on or after 1 July 2020, or
 - ends on a day that is on or after 1 July 2020 if the reporting period ends on the exit date because the holder of the product ceased to hold the product on the exit date

Current issues

- **No early opt-in for PDSs** – which creates practical implementation issues about PDS rolls for multi-PDS issuers
 - ASIC won't move on this issue*
- **PDS cut-off date** (30 September 2020) issues:
 - Whether applies to PDSs 'issued' or 'given'? there should be a sunset date for compliance after the cut-off date, for comparability and to avoid 'gaming'
 - Knock-on consequences of super PDSs and platforms relying on MIS data

This will be resolved with the ASIC announcements of amendments to the LI
- **Performance fee (for interposed vehicles)** issues:
 - Can components be disclosed in the 'Additional explanation of fees and costs' section?
 - How is the 5 year average calculated?

Current issues – cont'd

▪ Derivatives:

- Do unchanged original definition of indirect cost of OTC derivatives (not used for hedging) have a concept of 'implicit transaction costs' or 'market impact costs', which are excluded from the 'transaction costs' definition? Are they management fees and costs or not included at all?
 - If so, then ASIC is not right in saying there is no change to its approach on derivatives
- Implicit transaction costs and market impact costs are not defined in the instrument [but defined in RG 97]
- What is an explicit transaction cost for a derivative? What does this cover, given the confused treatment?

Current issues – cont'd

- **Periodic statement** issues:
 - Discrepancy between 2020 PDS and 2021 periodic statement disclosure methodologies

Questions?





Harry New
Partner
T +61 3 9603 3559
harry.new@hallandwilcox.com.au



Vince Battaglia
Partner
T+61 2 8267 3223
vince.battaglia@hallandwilcox.com.au



Kitty Vo
Partner
T +61 2 8267 3742
kitty.vo@hallandwilcox.com.au

Thank you

smarterlaw.com.au

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